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Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

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In the Matter of		
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Amendment of Part 20 and 24 of the Commission's Rules -- Broadband PCS Competitive Bidding and the Commercial Mobile Radio Service Spectrum Cap	)	WT Docket No. 96-59
	)	
Amendment of the Commission's Cellular PCS Cross-Ownership Rule	)	GN Docket No. 90-314

PETITION FOR RECONSIDERATION OF OMNIPOINT CORPORATION

Introduction and Summary

Omnipoint Corporation ("Omnipoint"), by its attorneys, files this petition for reconsideration of the June 24, 1996 Report and Order in the above-captioned dockets.[1] Omnipoint urges the Commission to reinstate one of the key principles of the entire PCS proceedings over the past eight years by reestablishing its rule limiting in-region cellular providers from acquiring more than 10 MHz of PCS spectrum until the year 2000. 47 C.F.R. § 24.204(a).

In-region cellular operators possess enormous market advantages over start-up PCS providers. Indeed, the success of the Commission's goal for a more competitive mobile service

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[1] Report and Order, WT Dkt. No. 96-59, GN Dkt. No. 90-314, FCC 96-278, 61 Fed. Reg. 33859 (July 1, 1996) ("R&O").

market depends significantly not only on the ability of new entrants to obtain sufficient licensed spectrum to compete with cellular incumbents; but, regulations to encourage competition in mobile services must also prevent or delay the incumbent duopoloists from exploiting their extraordinary advantages over PCS entrants. For these reasons, since 1993, the Commission's PCS band plan has limited in-region cellular operators from acquiring more than 10 MHz of in-region PCS spectrum in the auctions. The Commission concluded that a cap of 10 MHz until the year 2000 for any in-region cellular providers was an appropriate limit because it would prevent cellular incumbents from capturing spectrum to the disadvantage of new entrants.

At the 23rd hour, just as the PCS allocation process is about to close, and after many entrepreneurs have paid hundreds of millions of dollars to compete under one set of rules, the Commission's R&O effectively reverses from three years of established policy for mobile services competition. This extraordinary change is largely in reaction to the opinion in Cincinnati Bell Telephone Co. v. FCC, 69 F.3d 752 (6th Cir. 1995), which did not recommend that the Commission make such a change. In the R&O, the Commission eliminated the 10 MHz in-region restriction and relied on a Herfendall-Hirschman Index ("HHI") analysis to justify its conclusion that a 45 MHz cap alone "adequately addresses our concerns about anticompetitive behavior." R&O, at ¶ 104. However, the assumptions underlying the Commission's HHI analysis are seriously flawed and leave no reasoned basis for the Commission's decision to alter the existing band plan which has stood for three years and upon which many mobile service operators and investors have relied. On reconsideration, the Commission should return to the cornerstone of its policy for PCS -- the promotion of new mobile services competition -- by reinstating its cellular eligibility restriction.

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I. The R&O Fails to Address Legal and Market Considerations As It Expands the Domination of Cellular In the Mobile Services Market

The FCC, in its R&O, articulates three reasons for changing the existing cellular eligibility rule. First, at ¶ 94, the Commission vaguely refers to its "concern" about the Cincinnati Bell decision. Of course, Cincinnati Bell did not direct the Commission to change the PCS band plan and, as discussed below, the court even found that the Commission has full authority to impose a variety of rational spectrum cap limits as between competing mobile providers. Second, the R&O, at ¶¶ 96-100, relied on a "simple" HHI analysis (after having rejected an anti-trust analysis as applied to the cellular/PCS spectrum cap[2]); too simple, in fact, because it completely avoids consideration of the reasons that the cellular eligibility cap was adopted -- the fact that PCS operators must enter a market in which cellular has enjoyed a ten-year duopoly head start. Even if one takes the HHI analysis at face value, it demonstrates that (1) the current mobile service market, which cellular dominates, exhibits "extremely high concentration," R&O at ¶ 98, and (2) the rule change moves the mobile service market only from "extremely high concentration" to "high concentration," either of which is cause for concern under FTC/DOJ Guidelines. On the basis of those results, the R&O remarkably decides that the rule change "adequately addresses our concerns about anticompetitive behavior." R&O at ¶ 104. Finally, the R&O, at ¶ 105, noted that because of the vigorous competition for PCS licenses in the auctions, "it is appropriate to relax our PCS ownership rules" because more opportunities to own interest in other in-region providers will somehow "enhance[] opportunities to compete." Vigorous auction competitors and vigorous new competitors in mobile services, however,

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2 See, Third Memorandum Opinion and Order, GN Dkt. 90-314, 9 FCC Rcd. 6908, 6913 ¶ 31 (1994) ("Third MO&O").

depend to a large extent on the ability of new entrants to compete *against* the incumbent cellular provider.

A. Significant Reliance Interests Caution Against Changing the PCS Band Plan in the Wake of Cincinnati Bell

From its initial order establishing the regulation and spectrum band plan for PCS,[3] the Commission has laid down a consistent policy that its PCS regulations must proactively promote new mobile entrants because of cellular's domination of the current mobile service market. With the Commission's decision to allocate 120 MHz of spectrum for PCS and the Congressional directive to auction that spectrum in a manner that "avoid[s] excessive concentration of licenses," 47 U.S.C. § 309(j)(3)(B), the Commission appropriately addressed two primary goals in implementing the PCS band plan: (1) avoiding the potential for incumbent cellular providers to acquire PCS spectrum in the auction and effectively block new competition in an anticompetitive manner, and (2) ensuring in a proactive manner that the initial allocation of spectrum is designed to favor the new entrant.[4] *See, e.g.*, Third MO&O, 9 FCC Rcd. at 6913 ¶ 31 (cellular eligibility "rules reflect a balance of many public interest considerations, including the need to provide parties other than cellular licensees an opportunity to participate in PCS."). The Commission has substantially reaffirmed its initial commitment to the principle of PCS/in-region cellular

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3 Second Report and Order, GN Dkt. No. 90-314, 8 FCC Rcd. 7700 (1993) ("Second R&O").

4 While the opinion of the Cincinnati Bell court unfairly characterized the Commission as "waffling" between the goals of prevention of anticompetitive behavior and promotion of new competition, 69 F.3d at 762, these goals are complimentary. In the context of the cellular market with "extremely high concentration," the creation of new competition in mobile services curbs anticompetitive behavior.

eligibility restrictions in two subsequent reconsideration proceedings. Second R&O; Memorandum Opinion and Order, GN Dkt. 90-314, 9 FCC Rcd. 4957 (1994); Third MO&O.

The Commission should not, as it apparently has done in the R&O, lightly overrule its PCS band plan at this critical point in the development of PCS. Operators have either paid or committed to pay the government over $15 billion dollars for the right to use the PCS spectrum, relying on every aspect of the PCS regulatory scheme, including the cellular eligibility rules, in their business plans. Omnipoint alone has committed to pay over $750 million dollars in license fees for the right to compete against some of the largest telecommunications companies and consortia of such companies, including the existing in-region cellular incumbents. The prices paid, the investments made, and the market strategies that are already set are dependent on the stability of the Commission's band plan.[5] The Commission did not address this reliance issue in its determination to change its cellular eligibility rules in the R&O, and certainly did not give it the consideration that the courts have indicated it deserves. *See* National Ass'n of Independent Television Producers & Distributors v. FCC, 502 F.2d 249, 255 (2d Cir. 1974); Bowen v. Georgetown Univ. Hosp., 488 U.S. 204, 220 (1988 (Scalia, J., concurring) (indicating that an amended rule "that makes worthless substantial past investment incurred in reliance upon the prior rule . . . may for that reason be 'arbitrary' or 'capricious,' . . . and thus invalid."); Sixth Report and Order, PP Dkt. No. 93-253, 11 FCC Rcd 136 ¶ 16 (1995) (Commission retains PCS Block C 49% equity exception in response to Supreme Court's Adarand decision in order to

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5 The Commission has also reported to Congress that its 10 MHz cellular eligibility restriction is one of several "rules for broadband PCS . . . designed to promote competition." "Annual Report and Analysis of Competitive Market Conditions with Respect to Commercial Mobile Services", First Report, 10 FCC Rcd. 8844 8860 (1995) ("First Report on CMRS Competition").

"help preserve existing business relationships formed in reliance on our prior rules"), *aff'd*, Omnipoint Corp. v. FCC, 78 F.3d 620 (D.C. Cir. 1996).

The Cincinnati Bell decision provides no basis for the Commission to alter these policy goals. To the contrary, the court found that the Commission does have statutory authority, pursuant to 47 U.S.C. § 309(j)(3)(B), to impose spectrum caps "to promote competition and avoid undue concentration of licenses." Cincinnati Bell, 69 F.3d at 762. With this authority, the Commission is also empowered to impose spectrum caps that vary from service to service due to "different characteristics of the two markets." Id. at 765. Because PCS and cellular could not be more different in terms of market share, infrastructure development, control over distribution channels, and operational experience, the Commission's original policy favoring distinct cellular/PCS eligibility rules is buttressed by the court's opinion.

On remand, the Cincinnati Bell court only required the Commission to provide reasoned economic support for cellular eligibility restrictions. Id. Careful examination of the record in this proceeding demonstrates that such support already exists. *See*, Section II, below. Moreover, the R&O's adoption of a new band plan is arbitrary because of the faulty application of HHI analysis. *See*, Section I(B), below.

B. The Commission's Economic Analysis Ignores Significant Market Factors and Fails to Provide Support For Its Rule Change

1. The HHI Analysis Ignores Significant Market Considerations

The FCC improperly assumed that capacity measured in terms of spectrum held by the licensee is an appropriate measure of market share as between PCS licensees and in-region cellular operators. R&O at ¶ 96, fn. 286. The DOJ/FTC Guidelines indicate that market share should be calculated "using the best indicator of the firms' future competitive significance." 1992 Department of Justice - Federal Trade Commission Horizontal Merger Guidelines, 4 Trade Reg. Rep. (CCH) at ¶ 1.41 ("DOJ/FTC Guidelines"). Physical capacity is used only if it is the most effective measure that distinguishes competitors from one another. Id. The DOJ/FTC Guidelines also state that the relevant participants in the market for an HHI study generally includes only those firms "that currently produce or sell in the relevant market." DOJ/FTC Guidelines, ¶ 1.31. By contrast, the FCC's choice of licensed spectrum as the measure of market share is inappropriate because PCS licensees will not have any good or service to provide upon licensure; unlike in-region cellular incumbents, PCS licensees are not market participants and do not obtain market share simply by virtue of holding a spectrum license.

The issue of *when* one evaluates the level of concentration in the mobile services market is critical to evaluating the cellular eligibility rule, and yet it was completely overlooked in the Commission's analysis. As Omnipoint and others have consistently stated, the cellular eligibility rule is a temporal restriction that applies only for the next three years -- the period that PCS operators need to acquire the necessary spectrum and build-out their systems. It is beyond dispute that a PCS operator does not obtain customers or operating revenues with the issuance of its CMRS license. It takes at least a year or longer for a PCS operator in any major market to even begin commercial testing of its system and, as evidenced by build-outs to date, it requires approximately 18 to 24 months for most PCS operators. At that point, the PCS operator has no customers and has not deconcentrated the mobile market at all.[6] It is equally apparent that PCS will not obtain significant market share vis-a-vis cellular for several years to come. Currently, there are only five out of the 493 BTA markets with operating commercial PCS systems: in 99% of the BTA markets there is no PCS service yet.

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6 Evidence of the FCC's misplaced focus on the long-term is also demonstrated at ¶ 99 of the R&O, in which the Commission states that allocated spectrum "is a measure of a CMRS carrier's long-term capacity and is easily available to the Commission."

The Commission's focus on spectrum as a measure of market share would suggest that a small business Block C applicant today, who has yet to even receive its license(s), holds more market share than the in-region cellular operator. Since the Commission's economic analysis was intended to measure the effect of maintaining the 35 MHz cellular eligibility restriction only until the year 2000, it is plainly inappropriate to evaluate the market during that time frame under the assumption that a 30 MHz PCS operator is a *more* significant market participant than a 25 MHz incumbent in-region cellular operator.

The Commission cites United States v. General Dynamics Corp., 415 U.S. 486 (1974) to support its use of spectrum as a measure of capacity. There, the *operating* company's ability to compete in the coal supply business was measured by coal reserves, because a company with a large supply of its tangible good in stock could have greater influence in negotiating a supply contract. But, General Dynamics does not indicate that capacity should apply here, where PCS operators must overcome more than just capacity issues to effectively compete in the market.[7] The General Dynamics court appropriately considered only those competitors actually providing a service in the coal market, not all owners of land which contained coal reserves irrespective of whether those owners could actually bring that coal to market. Similarly, the Commission should focus its economic analysis on the state of mobile service competition offered by current providers. The General Dynamics case instructs, , that "[e]vidence of the amount of annual sales is relevant as a prediction of future competitive strength, since in most markets distribution systems and brand recognition are such significant factors that one may reasonably suppose that a company which has attracted a given number of sales will retain that competitive strength."

7 Moreover, in General Dynamics coal reserves as a measure of market share was appropriate only because the coal supply business operates on long-term requirements contracts, which effectively limit a supplier's ability to react to changes in demand through its coal reserves. General Dynamics, 415 U.S. at 501-02.

General Dynamics, 415 U.S. at 501. Applying this general rule here, it is clear that in-region cellular incumbents have the additional advantages of brand recognition, an exclusive lock on major distribution channels, and a strong customer base, and therefore their capacity represents substantially more market share than the Commission estimated.

Finally, we note that spectrum capacity for new entrants may not be devoted to mobile services at all. Under the Commission's recently adopted order in "Amendment of the Commission's Rules to Permit Flexible Service Offerings in CMRS," WT Dkt. No. 96-6, CMRS licensees may devote any proportion of their spectrum, including all of their spectrum, to the provision of fixed services in competition with wireline providers. New entrants, as opposed to cellular providers with an existing mobile customer base, and infrastructure to service mobile customers, are more likely to enter the fixed wireless market. Therefore, the assumption that PCS spectrum capacity will be used for mobile services is speculative, at best. Since in most markets the monopoly LEC is also one of the two in-region cellular operators, the R&O shifts enormous power over to the incumbent to block the entry of fixed wireless local loop services.

2. The HHI score indicates impermissibly high market concentration

The FCC staff performed an HHI analysis of various market situations, including the 45 MHz scenario, which received a score of close to 1900. As the Commission appropriately noted in the R&O, at ¶ 96, "an HHI over 1,800 shows a highly concentrated market, in which certain combinations 'are likely to create or enhance market power or facilitate its exercise' unless a strong showing to the contrary is made (citing DOJ/FTC Guidelines, § 1.51(a)-(c))." Because the Commission's efforts to make such a showing have failed, it must act to prevent unfair market conditions for new PCS entrants.

Despite the fact that it received a failing score, the FCC determined that "the 45 MHz CMRS spectrum cap is needed to prevent undue market concentration and the noncompetitive conditions in local markets that result from such concentration." R&O at ¶ 98. The Commission based its determination that the 45 MHz cap would improve competition on at least two flawed assumptions: (1) it compared the 45 MHz cap to the existing two-competitor market rather than the alternative market scenarios with 6 or more competitors, and (2) it identified as additional mitigating HHI factors the existence of other communications services that are "cross elastic" with PCS, including CB radio and local exchange service. R&O at ¶ 100.

The comparison between the existing market situation of two cellular incumbents, which has an HHI score of 5500, and the 45 MHz scenario is disingenuous because the favorable comparison is created by the fact that *more entities will own licenses after the auction.* This is radically different than the Commission's implication that the favorable comparison was created by relaxing the spectrum cap for cellular incumbents. *See, e.g.*, R&O at ¶ 103. In fact, both the comparison and the mitigating factors that the FCC claimed further reduced the HHI score apply equally to a situation in which in-region cellular incumbents are initially limited to 10 MHz of the PCS spectrum. There is no evidence cited in the R&O that these benefits relate to the selection of 45 MHz as the new limit.

Further, a proper market HHI analysis focuses on the narrowest possible group of relevant substitute goods or services. DOJ/FTC Guidelines, ¶ 1.11. The mitigating factors identified in the DOJ/FTC Guidelines include changing market conditions, such as new technologies (which cellular entities are just as able to innovate as PCS entities), or the existence of "close" substitutes for a good or service. DOJ/FTC Guidelines, ¶ 1.522. Accordingly, it is inappropriate to use the existence of paging services, CB radio services, landline services, maritime service, and private radio service as a mitigating factor for the high HHI level. These services are not substitutes for commercial broadband mobile service as they do not offer comparable voice transmission, geographic coverage, mobility, or quality or security of service.

At best, the FCC has identified a problematic competitive situation and attempted to solve the problem by creating a new problematic competitive situation benefiting only the cellular incumbents. The Commission should be seeking, and has the opportunity to create, a more competitive marketplace. The R&O states, at ¶ 101, that "cellular operators have a competitive position that is superior to that of any new market entrant. They also have strong incentives to preserve that existing advantage." Given the fact that the HHI analysis proves nothing more about the 45 MHz cap than it also proves about the 35 MHz cap, and given Commission recognition of the cellular provider's competitive advantage and anti-competitive motivation, its relaxation of the spectrum cap is baffling and should be reconsidered.

C. Increasing the Spectrum Cap will Threaten Competition

The HHI analysis ignores the relevant market differences between cellular and PCS operators. By neglecting these differences, the Commission incorrectly concluded that a relaxation of the traditional rules would enhance competition. A review of the technical and economic realities facing new PCS entrants, however, supports the previous 35 MHz cellular eligibility restriction.

In assessing the mobile services market, and its decision to abandon the 35 MHz cellular eligibility restriction, the Commission overlooked numerous cost and operating factors that are unique to PCS operators:

Spectrum Costs: Leading PCS entrants must each pay hundreds of millions of dollars for spectrum blocks prior to building out their systems. These are fixed costs that many cellular incumbents did not face in the past. Further, cellular incumbents can use their duopoly profits to subsidize their expansion into PCS.

Cell Site Locations: The ten year cellular head start has provided in-region incumbents with access to the most advantageous site locations for base stations. PCS operators must quite often settle for inferior site location and face tremendous competition for available sites. With an increase of local government zoning restrictions and delays against PCS operators, the in-region's site location advantages are a commodity not shared by PCS new entrants.

Microwave Incumbent Interference: As the Commission well knows, the relocation of microwave incumbents has been and will continue to be costly both in terms of time and financial resources. Despite relocation or the possibility of spectrum sharing, studies have indicated that interference is both likely and that it will be costly. *See, e.g.*, First Report on CMRS Competition, 10 FCC Rcd at 8860 (PCS "spectrum is currently encumbered and must be cleaned before it can be used effectively."). While all auction participants may have to negotiate with and relocate microwave incumbents, only new PCS entrants must put their business plans on hold because the cellular incumbents already have clear spectrum. Perhaps more importantly, one of the original purposes of the 10 MHz Block D, E, and F allocations was to enable a 30 MHz or 10 MHz PCS operator to obtain an additional 10 MHz and thereby engineer around incumbent OFS operators. Under that intended purpose of the PCS band plan, competitive PCS services could be brought to market sooner. Allowing each in-region cellular operator to own 20 MHz will effectively foreclose the original purpose for the 10 MHz licenses.

Cellular Customer Embedded Base: In-region cellular's status for ten years as the duopoly provider of mobile services gives it a tremendous embedded customer base. Virtually all cellular customers are under long-term contracts and thus have serious barriers to switching to a competitive PCS offering. PCS operators offering mobile services must effectively market to draw existing cellular customers away, which is a tremendous market advantage for the incumbent. Additionally, as indicated in the General Dynamics case above, the brand recognition of the incumbents is an invaluable asset in determining its potential to capture market share.

1.9 GHz Propagation Characteristics: As the Commission itself has noted, "because of the propagation characteristics of the broadband PCS frequencies, many more cells and base stations will be required than for cellular." First Report on CMRS Competition, 10 FCC Rcd. at 8860. Thus, cellular operators may achieve an overall system build-out cost that is lower than a purely PCS competitor.

Number Exhaustion: Many regions in the country are experiencing number exhaustion or near exhaustion of number resources. These crises areas make it very difficult or impossible for new entrants, including PCS operators, to obtain the numbers they need to launch their service. Cellular carriers, that have an existing base of numbers and that do not need a new number for every subscriber, are less adversely affected by this issue.

Exclusive Distribution Channels: Cellular operators have tied up exclusive arrangements with most major retail outlets selling mobile hand-sets prior to the time that PCS operators were even licensed. This fact alone renders the Commission's HHI analysis woefully inadequate.

II. The Cellular 35 MHz Restriction Better Serves the Public Interest

The in-region cellular eligibility rule was crafted to allow new entrants in the mobile service market to acquire the spectrum they need to launch a competitive PCS system. Memorandum Opinion and Order, GN Dkt. No. 90-314, 9 FCC Rcd. 4957, 4979 (1994) (changing FCC license allocations from 20 to 30 MHz in order to encourage rapid introduction of service, avoid incumbent microwave relocation costs, and facilitate economies of scale); id. at 4981 ("we believe that some new entrants may need to acquire 40 MHz to fully realize their business plans . . . ").

By definition, in-region cellular incumbents do not share the same challenges as a PCS new entrant as discussed above. These problems unique to the successful implementation of

PCS new entrants, provide cellular in-region operators with an inherent advantage to capture both the Block D and E 10 MHz licenses.[8] Coupled with the in-region provider's additional incentive to block new entrants from acquiring additional spectrum, the cellular operator in the Block D, E, and F auction would otherwise significantly undermine the Commission's statutory mandate to : " promot[e] economic opportunity and competition and ensur[e] that new and innovative technologies are readily accessible to the American people by avoiding excessive concentration of licenses and by disseminating licenses among a wide variety of applicants." 47 U.S.C. § 309(j)(3)(B).

The Commission's proceedings have established that, due to in-region cellular's market domination, "the CMRS business is not fully competitive;"[9] PCS entrants will be at a competitive disadvantage should cellular incumbents obtain 20 MHz of spectrum. The Commission's First Report on CMRS Competition offered independent findings of cellular market power that were not considered by the Cincinnati Bell court. The Commission found tell-tale indicia of a monopolistic industry. First, the prices of cellular offerings were substantially above competitive levels, as evidenced by recent significant price reductions in the face of competition.[10] Second, evidence indicates that cellular systems in major market areas "are earning economic rents of significant proportions."[11] Cellular firms in major metropolitan areas

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8 The Commission would also permit an in-region cellular operator to own up to 40% of the Block F entrepreneur

9 Annual Report and Analysis of Competitive Market Conditions with Respect to Commercial Mobile Services, First Report, 10 FCC Rcd. 8844. 8866, 8872 (1994) (the "First Report on CMRS Competition").

10 First Report on CMRS Competition, 10 FCC Rcd. at 8851-52, 8871-72.

11 Id. at 8871, 8884-88 (Tables 9 through 13)

would not be able to sustain such profit margins without the FCC's prior policies supporting such market power. Maintaining a 10 MHz cap on cellular acquisition of PCS spectrum at least until the year 2000 will help combat this competitive imbalance.

Respectfully submitted,

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